

New Zealand

More intense activity from private equity funds will lead to a more competitive M&A market with stronger multiples

Current Environment

The New Zealand economy continued to grow in 2006. Gross Domestic Product was up by 2.2% during the first quarter of 2006 and Real Gross National Disposable Income up 1.3% for the March 2006 year.

However in the last quarter of 2005, the economy showed its first quarter of negative growth in over four years. This slowdown had been long anticipated by economists; however the consensus is that it is likely to be a soft landing rather than a more severe turn for the worse.

Escalating housing costs and oil prices are the largest factors contributing to New Zealand's 3.3% inflation rate (fiscal year to March 2006). However, all-time oil price peaks have spurned overseas interest in drilling off the coastlines of New Zealand.

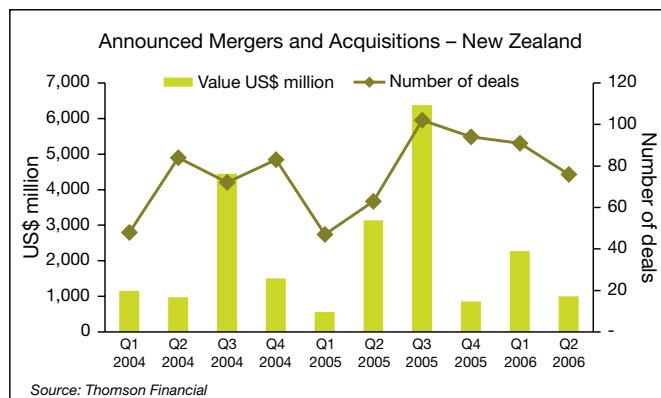
Real private consumption is expected to continue to grow, albeit at a reduced rate from that experienced recently. This growth is expected to continue despite increased oil prices, as a result of a combination of factors including: low unemployment and real wage growth; a forecast decrease in interest rates towards the end of the calendar year; the introduction of income support packages targeted at middle-income earners; and the solid state of household balance sheets.

The New Zealand budget for 2006 (Budget 2006) allocated new operating spending of NZ\$9.6 billion (US\$6 billion) and capital of NZ\$2.7 billion (US\$1.7 billion) over the next four years. The most significant focus for these new monies is transport infrastructure, including funding for New Zealand's largest ever road building programme, for which roughly NZ\$1.3 billion (US\$800 million) was set aside for the next five years to guarantee the State Highway programme and accelerate critical road projects, such as Auckland's Western Ring Route, Waikato's Expressway and Wellington's Western Corridor. A number of important regional projects will also be fast-tracked.

The Budget 2006 significantly expanded support for exporters keen to break into offshore markets with a NZ\$64 million (US\$40 million) increase to the market development scheme as New Zealand pushes towards a more significantly export-led economy.

The Budget 2006 also set aside NZ\$60 million (US\$37 million) of new capital funding for the Venture Investment Fund (VIF) over the next three years, with the possibility of another NZ\$40 million (US\$25 million) over the following two years, depending on an evaluation in 2009. The VIF invests in innovative New Zealand businesses and aims to accelerate development of the New Zealand venture-capital industry through co-investment with private investors, by increasing the level of early stage investment activity in the New Zealand market.

Deal Activity



Australian based Private Equity firms continued their search for acquisitions as their presence in the New Zealand M&A market increased. Recent transactions and deal multiples demonstrate that Private Equity firms are prepared to pay full value for well established, mature businesses with global growth aspirations.

Most notable over the time period was Pacific Equity Partners' acquisitions of the food businesses Griffins, for NZ\$390 million (US\$240 million) and Tegel for NZ\$250 million (US\$155 million). The high deal multiples and prevalence of private equity in the New Zealand M&A context is partially a function of the significant growth in available funds in the Australasian market, coupled with maturing debt markets. These two factors have led to an increase in the volume of deals in first half of 2006 by 26%, compared to the same period last year.

Unlike 2005, in which there was strong interest in the Aged-Care and Health sectors, 2006 has seen consumer staple companies coming to the fore. Two emerging sectors for the second half of 2006 appear to be building products and finance. Already we have seen Next Capital purchase Hirepool (New Zealand's largest equipment hire company), a business valued at NZ\$172 million including debt (US\$107 million). Consolidation within the finance sector looks likely as investors shift towards quality finance companies, following the recent receiverships of National Finance 2000 and Provincial.

Other significant deals over the last six months include:

- The sale of the food business Uncle Toby's by Burns Philp to Nestle for NZ\$1.1 billion (US\$680 million)



- Transpacific's merger with Waste Management for NZ\$870 million (US\$540 million). This deal received much attention as a number of commentators felt that takeover rules were being sidestepped, when the board of Transpacific and Waste Management Classified the deal as a 'merger' as opposed to a 'takeover'. Under the New Zealand Takeovers Code, the compulsory acquisition provisions can be effected via merger by the higher threshold of owning a 75% majority of voting rights, as opposed to 90% in a takeover
- Fairfax's acquisition of TradeMe, a privately held New Zealand internet auction website, for NZ\$750 million (US\$470 million) was the most talked about transaction in the first half. The large price tag for the young internet/ media company represented a multiple of almost 15 times forecast EBITDA

Outlook

The long awaited correction to the New Zealand dollar against the US and Australian dollars has finally occurred with a 13% and 9% decrease, respectively against these currencies.

The sharp decline in the New Zealand dollar has made New Zealand a more attractive home for international investment.

The fall in the dollar was also a welcome relief for exporters and the economy, although it has yet to be fully reflected in New Zealand's current account or gross domestic product (GDP).

New Zealand's real GDP growth rate is expected to ease to around 0.8% for the remainder of the fiscal year to March 2007, rebounding to 2.0% and 3.3% in 2008 and 2009, driven by healthy trading partner growth and the impact of the lower dollar on exporter returns. Unemployment is forecast to increase only slightly to around 4-5% over the next two years. The tightness in the labour market is expected to remain for the next four years resulting in a real wage growth drive.

We expect M&A activity to continue to be strong over the next twelve months. In particular, private equity firms will to continue their expansion into New Zealand, driving industry rationalisation and further diversifying their portfolios. These firms are certainly no longer sideline players picking up underperforming assets, but are now viewed as serious players, frequently outbidding trade buyers. The pressure this puts on bidding competition suggests that transaction multiples will remain strong.

